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C O N F I D E N T I A L SECTION 01 OF 02 OTTAWA 003765

SIPDIS

NOFORN

DEPARTMENT FOR EB/IFD/OMA, AND WHA/CAN

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TAGS: EFIN ECON PREL CA SIPDIS

SUBJECT: OPPOSITION PARTIES SEIZE ON RCMP INVESTIGATION OF POSSIBLE LEAK FROM DEPARTMENT OF FINANCE

REF: 04 OTTAWA 2822 (IMETS)

Classified By: Classified by Curtis Stone, Acting Economics Minister Co unselor, Ottawa. Reason: 1.4(b) and (d).

11. (U) Summary: Opposition parties have seized on confirmation of an RCMP criminal investigation into the possible leak of tax information from the Department of Finance, calling for Finance Minister Ralph Goodale to resign. Goodale, reiterating his confidence that he, his political staff, and officials at the Finance Department will be cleared, has said he does not intend to step aside. The story led the national news and was carried in front, not business, sections of the newspapers but it is too early to tell if this will affect the outcome of the January 23 election. End summary.

12. (U) In a letter to NDP Finance Critic Judy Wasylycia-Leis, Commissioner Giuliano Zaccardelli confirmed that the Royal Canadian Mounted Police (RCMP) will investigate "a possible breach of security or illegal transfer of information in advance of the federal government's announcement of changes to the taxation of Canadian corporate dividends and income trusts Nov. 23, 2005." He added that there is no evidence of wrongdoing by anyone including Mr. Goodale.

What happened?

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13. (U) The investigation arose from a request by Wasylycia-Leis, who was concerned about a surge in trading in the hours before Minister Goodale announced his new policy. On November 23, after markets closed, Minister Goodale announced that he had decided not to tax investment trusts but would cut taxes on corporate dividends to reduce the advantage that income trusts had enjoyed in the market. The GOC has long expressed concern about the surge in the tax-advantaged income trusts and was widely expected to increase taxes on those instruments.

14. (U) Goodale's announcement was preceded by unusually heavy trading and sharp increases in the price of financial instruments that would benefit from the new policy. A forensic accountant who examined the trading records told the press that he would guess "there was an over 90 per cent probability of insider trading" and that the case requires an investigation. Canada's Association for the Fifty-Plus (CARP) has vigorously denied a TV report that it received a call on November 23 from the Liberals reporting that something was going to be said (about income trusts).

Campaign Windfall for the Opposition

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15. (U) Wasylycia-Leis has asked that Goodale step aside as Finance Minister and the Conservative party is also calling for Goodale's resignation. When allegations of a leak first arose, Minister Goodale stated that he was confident that neither Finance officials nor his ministerial staff leaked the information. He confirmed December 28 that "I have looked at this situation very carefully and I am absolutely confident about my conduct in this matter and I do not see any basis on which to resign." With over three weeks to go in a hard-fought election campaign, the Minister is not in Ottawa these days, or involved in policy decisions at Finance.

What next?

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16. (U) Commissioner Zaccardelli has confirmed that the RCMP is investigating the possible leak. This type of investigation is likely to be handled by the Commercial Crimes section rather than the Integrated Market Enforcement Teams (reftel), although they might call on the IMET for expertise.

17. (U) Market Regulatory Service (MRS) is the regulatory body with jurisdiction in this case. MRS was created when the Toronto Stock Exchange was privatized and has

responsibility for monitoring the markets. Self regulatory organizations such as the Investment Dealers Association would not be likely have a role in the investigation.

¶ 18. (C/Noforn) The Ontario Securities Commission (OSC) has not said publicly whether it is investigating the complaint (although it was requested to do so by the Conservative party), but the OSC manager of Surveillance Enforcement (please protect) told us this is not an insider trading case as the Minister, and Finance officials, do not have a "special relationship" with the traders. Although he was reluctant to discuss the case, he said the OSC could take action on public interest grounds "if it (the leak) happened" but would need to establish a profit motive (presumably by the leaker). He confirmed that Federal officials are not "issuers" subject to OSC regulation. Comment: The OSC would clearly like to steer clear of this controversy. End comment.

¶ 19. (C) At the Department of Finance, the issue of taxation of dividends and income trusts was handled by officials in the Financial Sector Branch, the Tax Branch, and of course by the Minister's staff and the communications office. A high-level public servant at Finance said the investigation has not had an impact on his staff yet, although he expects "the RCMP will be around to talk to us." He is confident that, if there was a leak, it was not from bureaucrats at Finance. "I know the people here and know how they handle things, and we handle much more sensitive things routinely" (without leaks).

¶ 10. (C/Noforn) Comment: This investigation joins the Dingwall affair and the sponsorship scandal in cementing the image of Liberal Party entitlement and corruption, although the Opposition may be jumping a bit prematurely as the investigation is still in a very early stage. (Conservative Party Leader Steven Harper, contradicting his party's official press release, said at a press conference today that he personally hopes Goodale doesn't resign, but continues to campaign as a symbol of Liberal corruption.) While the impact on voters is not clear, the investigation's timing, following recent embarrassing gaffes by Liberal staffers, is just one more negative for a party trying to dig out from under the perception of corruption revealed by the sponsorship scandal.

¶ 11. (C/Noforn) Comment continued: Whether or not there was wrongdoing involved, the politically inept handling of the issue of taxing income trusts in one in a series of decisions on which the Liberal party has stumbled. There had been criticism that the popularity of income trusts reflected the need to revamp the entire corporate tax system rather than focusing on penalizing one product. The November 23 decision was preceded by what one columnist described as the Liberals "sending mixed signals, dithering, contradicting themselves." The long-delayed clarification on bank mergers is another example of a decision that has significant financial sector ramifications but successive governments have chosen inaction and ambiguity over clear policy making.

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